(15)

No. 96-1578

IN THE

Supreme Court of the United States

OCTOBER TERM, 1996

HON. THOMAS R. PHILLIPS, ET AL.,
Petitioner,

v.

WASHINGTON LEGAL FOUNDATION, ET AL.,
Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF OF AMICI CURIAE IN SUPPORT OF THE PETITIONERS

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IN THE SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1996

No. 96-1578

HON. THOMAS R. PHILLIPS, HON. RAUL A. GONZALEZ, HON. JACK HIGHTOWER, HON. NATHAN L. HECHT, HON. LLOYD DOGGET, HON. JOHN CORNYN, HON. BOB GAMMAGE, HON. CRAIG T. ENOCH, HON. ROSE SPECTOR, TEXAS EQUAL ACCESS TO JUSTICE FOUNDATION, AND W. FRANK NEWTON, IN HIS OFFICIAL CAPACITY AS CHAIRMAN OF THE TEXAS EQUAL ACCESS TO JUSTICE FOUNDATION, *Petitioners*,

v.

WASHINGTON LEGAL FOUNDATION, WILLIAM R. SUMMERS, AND MICHAEL J. MAZZONE, *Respondents*.

STATEMENT OF AMICUS INTEREST

The Commonwealth of Massachusetts and the undersigned 34 amici states have two direct interests in the resolution of this case. First, each of the amici states has an Interest on Lawyers Trust Accounts ("IOLTA") program. These IOLTA programs have been

created either by a state legislature or by a judicial order or rule of a state's highest court.[1]

The IOLTA programs have provided hundreds of millions of dollars that are principally directed to the provision of legal services to indigent families and individuals. In this way, states have secured significant financial assistance in addressing the states' important interests in the improvement of the administration of justice and the delivery of legal services to those who cannot afford them. If affirmed, the decision of the Fifth Circuit in this case would place the states' IOLTA programs in jeopardy.

The states' second interest concerns the proper application of the Fifth Amendment's Taking Clause, which requires that a state pay just compensation when it takes private property for a public use. In order to present a valid takings challenge, however, claimants must

[1] All fifty states and the District of Columbia have adopted IOLTA programs. The states implemented IOLTA programs on the following dates: Florida (1981); Idaho (1982); Maryland (1982); California (1983); Colorado (1983); Delaware (1983); Georgia (1983); Hawaii (1983); Illinois (1983); Minnesota (1983); Nevada (1983); New Hampshire (1983); New York (1983); North Carolina (1983); Oklahoma (1983); Utah (1983); Vermont (1983); Virginia (1983); Arizona (1984); Arkansas (1984); Connecticut (1984); Iowa (1984); Kansas (1984); Mississippi (1984); Missouri (1984); Nebraska (1984); New Mexico (1984); Rhode Island (1984); South Dakota (1984); Tennessee (1984); Texas (1984); Louisiana (1985); Massachusetts (1985); Montana (1985); Ohio (1985); South Carolina (1985); Washington (1985); Alaska (1986); Kentucky (1986); Maine (1986); Michigan (1986); Alabama (1987); New Jersey (1987); North Dakota (1987); Wisconsin (1987); Pennsylvania (1988); Oregon (1989); West Virginia (1989); Wyoming (1990). An IOLTA program in Indiana has been approved and is pending implementation. The District of Columbia implemented an IOLTA program in 1985. ABA/BNA, *Lawyers' Manual on Professional Conduct*, § 45:201 (1997).

first show that they have a property interest entitled to recognition under the Fifth Amendment. *Penn Central Transportation Co. v. New York City*, 438 U.S. 104, 124-25 (1978). In this case, the Fifth Circuit incorrectly determined that the plaintiffs have a constitutionally protected property interest in the interest generated in IOLTA accounts. An overbroad application of the term "property," such as is found in the Fifth Circuit's decision here, extends the protection of the Fifth Amendment beyond its intended scope, improperly exposing the states to unwarranted takings challenges.

SUMMARY OF ARGUMENT

The states have an important interest in improving the quality of legal services available to their residents. IOLTA programs significantly advance this goal by contributing funds for use in improving the administration of justice and delivering legal services to poor families and individuals.

The Fifth Circuit erred when it found that a client whose funds are placed in an IOLTA account has a constitutionally recognized property interest in the interest earned in that account. A client has no legitimate claim of entitlement to the interest earned in an IOLTA account since that interest is entirely a creation of the IOLTA program.

ARGUMENT

I. The States Have Important Interests In Providing Open Access To The Courts And In The Administration Of Justice.

Like the constitutions of many states, the Massachusetts Declaration of Rights sets forth the Commonwealth's important interest in providing free and open access to its courts:

> Every subject of the commonwealth ought to find a certain remedy, by having recourse to the laws, for all injuries or wrongs which he may receive in his person, property or character. He ought to obtain right and justice freely, and without being obliged to purchase it; completely, and without any denial; promptly, and without delay, conformably to the laws.

Mass. Const. pt.1, art.11.

The states also have an important interest in the administration of justice. *See, e.g.*, Cal. Bus. & Prof. Code Ann. § 6031(a)(West Supp. 1990)(broad statutory mission of the State Bar of California is to promote the administration of justice); and *Matter of Bar of Wisconsin*, 485 N.W.2d 225, 226 (Wis. 1992)(significant aspect of public interest is the efficient and effective administration of justice).

The important nature of these state interests has been recognized by this Court. In *Keller v. State Bar of California*, 496 U.S. 1, 14 (1990), the Court held that the State's interest in regulating the legal profession or improving the quality of legal services justified the compelled association which resulted from mandatory membership in the state bar. Likewise, in *Lathrop v. Donohue*, 367 U.S. 820, 842 (1961), the Court held that "improving the quality of legal service

available to the people of the State . . . is a legitimate end of State policy."

The money earned in IOLTA accounts provides significant assistance to the states in achieving these goals. Each year since 1990, the IOLTA programs combined have provided approximately $100,000,000 to charitable entities, typically non-profit legal organizations. The contribution of funds raised in IOLTA accounts has been especially important to the amici states during the past several years when funding for the Legal Services Corporation, which provides federal funds for legal services, has been significantly reduced.

Interest generated in IOLTA accounts has been used to assist the states in providing meaningful access to the justice system. In Massachusetts, for example, court rules regulating the IOLTA program require that the interest earned in IOLTA accounts be directed "for use in (1) improving the administration of justice or (2) delivering civil legal services to those who cannot afford them." Supreme Judicial Court Rule 3:07, Disciplinary Rule 9-102(c)(2)(a). Indeed, over 90% of the money earned in IOLTA programs nationally has supported the delivery of legal services, including pro bono legal services, to indigent families and individuals. Other activities supported by IOLTA funds include alternative dispute resolution programs, victim services programs, minority law recruitment programs, and law school scholarship programs. American Bar Association Commission on Interest on Lawyers' Trust Accounts, IOLTA Handbook (1997) at p.2.

Thus, the IOLTA programs make a substantial contribution toward achieving the goals of improving the administration of justice and providing civil legal services to low-income individuals who cannot afford to hire a lawyer. The importance of the IOLTA programs to the amici states and their indigent citizens cannot be overstated.

II. The Fifth Circuit Erred When It Determined That Clients Have A Property Interest In The Interest Generated In IOLTA Accounts.

With the exception of the Fifth Circuit's decision below, legal challenges asserting that IOLTA programs are unconstitutional have failed. The reason is simple: since IOLTA programs do not affect or impair any property interest of the client, there is no violation of the Fifth Amendment to the United States Constitution. All state courts that have decided the issue, as well as the First and Eleventh Circuit Courts of Appeals, have reached this conclusion. While the Fifth Circuit properly began its analysis by noting that "[s]tate law defines 'property'. . . ," *Washington Legal Foundation v. Texas Equal Access to Justice Foundation*, 94 F.3d 996, 1000 (5th Cir. 1996), the Court erred when it determined that the interest earned on IOLTA accounts is the property of the clients whose money is held in those accounts.

A. *Clients Whose Funds Are Placed In IOLTA Accounts Do Not Have A Reasonable Claim of Entitlement To The Interest Generated In Those Accounts.*

"Property interests, of course, are not created by the Constitution. Rather, they are created and their dimensions are defined by existing rules or understandings that stem from an independent source such as state law – rules or understandings that secure certain benefits and that support claims of entitlement to those benefits." *Board of Regents v. Roth*, 408 U.S. 564, 577 (1972). Thus, "a mere unilateral expectation or an abstract need is not a property interest entitled to protection." *Webb's Fabulous Pharmacies, Inc. v. Beckwith*, 449 U.S. 155, 161 (1980). Rather, a person must have "a legitimate

claim of entitlement" in order for an interest to qualify as a property interest for constitutional purposes. *Board of Regents*, 408 U.S. at 564. As this Court has noted, takings challenges have been dismissed even where a challenged governmental action caused economic harm, if the action did not "interfere with interests that were sufficiently bound up with the *reasonable* expectations of the claimant to constitute 'property' for Fifth Amendment purposes." *Penn Central Transportation Co. v. New York City*, 438 U.S. 104, 124-25 (1978) (emphasis added). *See also*, *Hooker v. Burr*, 194 U.S. 415, 419 (1904)(Constitution does not protect "abstract rights").

A client whose funds are placed in an IOLTA account cannot properly claim entitlement to the interest generated in that account because there is no reasonable expectation that that interest belongs to the client. This is because the interest generated by IOLTA client fund deposits is entirely a creation of the IOLTA program.

The Massachusetts IOLTA program is typical of IOLTA programs generally.[2] The Massachusetts IOLTA program is created by a rule of the Massachusetts Supreme Judicial Court.[3] Supreme Judicial

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[2] Variations in the IOLTA programs include whether the attorneys' participation in the program is mandatory or voluntary. *Compare*, New Mexico Rules of Court, Rule of Professional Conduct 16-115(D)(establishing voluntary IOLTA program) *with Petition of Minnesota State Bar Ass'n*, 332 N.W.2d 151 (Minn. 1982)(establishing mandatory IOLTA program). In addition, some programs include an opt-out provision, which provides that all lawyers must take part in the program unless they affirmatively give notice that they decline to participate. *See, e.g.*, Alabama Rules of Professional Conduct, Rule 1.15(f), (g).

[3] Forty-five of the IOLTA programs were created by an order of the respective state's highest court. The IOLTA programs in California, New York, Connecticut, Ohio and Maryland were created by the state legislature.

Court Rule 3:07 contains the "Canons of Ethics and Disciplinary Rules Regulating The Practice Of Law." Disciplinary Rule 9-102(C) regulates attorneys' handling of client funds. The Court rule neither requires clients to give any funds to attorneys nor requires attorneys to hold any funds for clients; it does not alter the relationship between lawyers and clients. The rule merely regulates the handling of some client funds that are accepted by attorneys.

Pursuant to this rule, if an attorney decides to accept client funds, those funds must be deposited into one of two types of interest bearing accounts. DR 9-102(C). Generally speaking, client funds are deposited in an individual client account with the interest payable as directed by the client. It is only those client funds held by the lawyer "which in the judgment of the lawyer are nominal in amount, or are to be held for a short period of time," that are to be deposited in an IOLTA account. *Id.* Interest from the IOLTA account is then paid, net of expenses, as directed by the attorney to a charity approved by the Supreme Judicial Court "for the use in (1) improving the administration of justice or (2) delivering civil legal services to those who cannot afford them." DR 9-102(c)(2)(a).

The funds pooled in IOLTA accounts are either so small or held for such a short period of time that it is not feasible to place them in separate interest bearing accounts. *Petition by Massachusetts Bar Ass'n*, 395 Mass. 1, 6, 478 N.E.2d 715, 718 (1985). Funds are deposited in an IOLTA account only if and when the lawyer determines that the administrative and transactional costs of placing the funds in a separate account exceed the interest likely to be generated. Previously, these client funds were typically placed in non-interest bearing checking accounts, where they could "benefit neither the attorney nor the client but simply redound[ed] to the benefit of the depository institution." *Id.* *See also*, ABA Formal Opinion 348 (1982), *reprinted in* 68 A.B.A. J.1502 (1982).

In these circumstances, where, in the absence of the IOLTA program, the client's funds would not earn interest payable to the client, a client has no reasonable claim of entitlement to the interest that is earned in an IOLTA account. Accordingly, the Fifth Circuit erred in this case when it determined that the plaintiffs have a constitutionally cognizable property interest.

B. *State Courts Have Appropriately Rejected Constitutional Challenges To IOLTA Programs.*

Each state court that has reached the issue of whether the regulation of interest earned by IOLTA programs constitutes a taking under the Fifth Amendment has determined that the clients whose funds were at issue did not have a constitutionally recognized property interest in the interest generated by these accounts.[4]

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[4] *See, Matter of Interest on Lawyers' Trust Accounts*, 283 Ark. 252, 675 S.W.2d 355 (1984), *rev'g*, 279 Ark. 84, 648 S.W.2d 480 (1983); *Carroll v. State Bar of California*, 166 Cal. App.3d 1193, 213 Cal. Rptr. 305 (Cal App. 4th Dist.), *cert. denied sub nom. Chapman v. State Bar of California*, 474 U.S. 848 (1985); *Matter of Interest on Trust Accounts*, 402 So.2d 389 (Fla. 1981); *Petition by Massachusetts Bar Ass'n*, 395 Mass. 1, 478 N.E.2d 715 (1985); *Petition of Minnesota State Bar Ass'n*, 332 N.W.2d 151 (Minn. 1982); *Petition of New Hampshire State Bar Ass'n*, 122 N.H. 971, 453 A.2d 1258 (1982); *Matter of Interest on Lawyer's Trust Accounts*, 672 P.2d 406 (Utah 1983); and *Matter of the Adoption of Amendments to CPR DR 9-102 IOLTA*, 102 Wash.2d 1101 (1984). While the Indiana Supreme Court declined to authorize an IOLTA program in *Matter of Indiana State Bar*, 550 N.E.2d 311 (Ind. 1990), that decision does not rest on constitutional grounds, but on an analysis of the Indiana Rules for Discipline of Attorneys and Rules of Professional Conduct. Indiana has subsequently approved an IOLTA program.

The Supreme Court of Florida was the first state court to determine that the earnings on clients' funds placed in IOLTA accounts are not "property" for the purpose of the Fifth Amendment. *Matter of Interest on Trust Accounts*, 402 So.2d 389 (Fla. 1981). There the court determined that "no client is compelled to part with 'property' by reason of a state directive, since the [IOLTA] program creates income where there had been none before, and the income thus created would never benefit the client under any set of circumstances." *Id.* at 395.

Subsequently, in *Carroll v. State Bar of California*, 166 Cal. App. 3d 1193, 213 Cal Rptr. 305 (Cal. App. 4th Dist.), *cert. denied sub nom. Chapman v. State Bar of California*, 474 U.S. 848 (1985), a California Court rejected a Fifth Amendment challenge to that state's mandatory IOLTA program. The *Carroll* court declined to recognize any client property interest in the interest generated by IOLTA accounts, reasoning that:

> [where] by definition, [the] transactional costs exceed or equal the total interest income generated, the clients suffer no loss for which they are entitled to compensation. The abstract right to control where interest earned on person's money may be funneled is not an economic right subject to monetary compensation.

213 Cal. Rptr. at 311.

Other state courts have followed the reasoning articulated by the Florida and California courts, finding that interest earned in an IOLTA account is not a property interest cognizable under the constitution. *See, e.g., Petition of Massachusetts Bar Ass'n*, 395 Mass. 1, 6, 478 N.E.2d 715, 718 (1985)("interest on nominal or short-term trust deposits held in trust accounts is not property for

constitutional purposes") and *Petition of Minnesota Bar Ass'n*, 332 N.W.2d 151, 158 (Minn. 1982)(no "property" is taken from client under IOLTA program).

Further, forty-five states have adopted IOLTA programs through an order or rule of the state's highest court. In approving the IOLTA program, these state courts have implicitly rejected the claim that the IOLTA programs are unconstitutional.

Accordingly, the state courts that have examined the issue have determined that clients are not deprived of "property" when nominal or short-term deposits are placed in IOLTA accounts. The state courts have consistently determined therefore that clients do not have a legitimate claim of entitlement in the interest earned in IOLTA accounts.[5]

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[5] The reasoning of the two other Circuit Courts of Appeals to have considered the issue is consistent with that of the state courts. In *Cone v. State Bar of Florida*, 819 F.2d 1002, 1007 (11th Cir.), *cert. denied*, 484 U.S. 917 (1987), the Eleventh Circuit held that the plaintiff did not have a legitimate claim of entitlement to the interest earned in an IOLTA program, reasoning:

> Here, there was no taking of any property of the plaintiff. Standing alone, her deposit in the IOTA account could not earn anything. By combining all such deposits, interest income has been created which was not within the legitimate expectations of the owner of any one of the principal amounts.

See also, Washington Legal Foundation v. Massachusetts Bar Ass'n, 993 F.2d 962 (1st Cir. 1993)(rejecting the claim that plaintiffs had a protected property right to exclude other from the beneficial use of funds deposited in IOLTA accounts).

C. *The Fifth Circuit Incorrectly Applied This Court's Reasoning In Webb's Fabulous Pharmacies, Inc. v. Beckwith.*

The Fifth Circuit rejected the reasoning of the courts cited above on the grounds that that reasoning did not give proper weight to this Court's decision in *Webb's Fabulous Pharmacies, Inc. v. Beckwith*, 449 U.S. 155 (1980). The Fifth Circuit's analysis of *Webb's*, however, is incorrect as it fails to recognize the express limitations of the scope of that decision.

In *Webb's*, this Court considered whether it was constitutionally permissible for a county to take the interest accruing on an interpleader fund deposited in the registry of the county court where a fee was also charged for the clerk's services in establishing the fund. The issue arose when a purchaser, who agreed to buy Webb's Fabulous Pharmacies, Inc. for over $1.8 million, discovered at the closing that Webb's debts appeared to be greater than the purchase price. *Id.* at 156. The purchaser filed a complaint of interpleader in the appropriate county court, interpleading Webb's and Webb's creditors and submitting the purchase price to the court. While the case was being resolved, the interest earned on the interpleader fund exceeded $100,000. *Id.* at 158.

The Court found that the creditors had a state-created property right to their respective portions of the fund. *Id.* at 161. After determining that the state had not offered any reasonable basis to support the taking of the interest earned by the interpleader fund, the Court found that the county had violated the Taking Clause of the Fifth Amendment. The Court, however, expressly noted the limited scope of its holding, stating:

> We hold that under the narrow circumstances of this case — where there is a separate and distinct state statute authorizing a clerk's fee "for services rendered" based upon the amount of principal deposited; where the deposited fund itself concededly is private; and where the deposit in the court's registry is required by state statute in order for the depositor to avail itself of other statutory protection from claims of creditors and others — Seminole County's taking unto itself, under § 28.33 and 1973 Fla. Laws, ch. 73-282, the interest earned on the interpleader fund while it was in the registry of the court was a taking violative of the Fifth and Fourteenth Amendments. We express no view as to the constitutionality of a statute that prescribes a county's retention of interest earned, where the interest would be the only return to the county for services it renders.

Id. at 164-65.

Ignoring the limited nature of the decision, the Fifth Circuit cited *Webb's* to support a general rule that a property interest exists in accrued interest "simply because '[t]he earnings of a fund are incidents of ownership of the fund itself and are property just as the fund itself is property.'" 94 F.3d at 1002 (quoting *Webb's Fabulous Pharmacies, Inc.*, 449 U.S. at 164). In reaching this conclusion, the Fifth Circuit overlooked significant factual distinctions between the interest that accrued on the interpleader fund in *Webb's* and the interest that is generated in IOLTA accounts. In *Webb's*, the $1.8 million that was placed in the interpleader fund during the resolution of the litigation generated over $100,000 of interest. Funds that are placed in IOLTA accounts, however, are either nominal in amount or are to be held for a short period of time so that, held individually, the funds would not net interest. While the creditors in Webb's may have had a reasonable expectation in the interest generated on the

interpleader fund, no such reasonable expectation exists for the clients whose funds are placed in IOLTA accounts.

Further, the Fifth Circuit's analysis cannot be reconciled with the Court's caveat concerning the limitation of its holding. Rather than developing a broad, general rule, this Court limited its holding to the "narrow circumstances of this case." 449 U.S. at 164. Indeed, the Fifth Circuit's approach is contrary to *Penn Central Transportation Co. v. New York City*, where the Court explicitly noted that it has not developed any "set formula" for determining whether a taking has occurred, looking instead to the particular factual circumstances of each case. 438 U.S. 104, 124 (1978).

Finally, the Fifth Circuit's reading of *Webb's* is inconsistent with the Court's statement that "[w]e express no view as to the constitutionality of a statute that prescribes a county's retention of interest earned, where the interest would be the only return to the county for services it renders." *Webb's Fabulous Pharmacies, Inc.*, 449 U.S. at 165. Thus, contrary to the general rule adopted by the Fifth Circuit in this case, the *Webb's* court acknowledged that in some circumstances, it may in fact be appropriate for the government to retain interest earned on privately held principal. Consistent with the reasoning in *Webb's*, such a result would depend upon whether the particular facts allowed the claimants to form a legitimate expectation in that interest. Inasmuch as the claimants in this case had no reasonable expectation in the interest generated in IOLTA accounts, the state court have appropriately rejected the constitutional challenges to the IOLTA programs and the Fifth Circuit's decision, based on a misapplication of the term "property," should be reversed.

CONCLUSION

For the foregoing reasons, the amici states respectfully request that the Court reverse the Fifth Circuit decision in this case.

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